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October 29, 2004

Ms. Marlene Dortch
Secretary
Federal Communications Commission
445 12th Street, SW, TW-A325
Washington, DC 20554

Re: Sunset of the BOC Separate Affiliate and Related Requirements, WC Docket No. 02-112, CC Docket Nos. 00-175, 01-337, and 02-33

Dear Ms. Dortch,

On October 29, 2004, the undersigned and Lyn Haney of BellSouth, Michelle Thomas, Brett Kissel, Chris Heiman, and Terri Hoskins of SBC, and Joe DiBella and Tom Moynihan of Verizon met with William Dever, Michael Carowitz, Bill Kehoe, Jon Minkoff, Pam Megna, Daryl Cooper, and Kim Jackson of the Wireline Competition Bureau.

The purpose of the meeting was to discuss in more detail the companies' proposed implementation of Section 272(e)(3) summarized during a previous *ex parte* meeting. (*BellSouth ex parte in Dkts 02-112, 00-175, 01-337, and 02-33, filed October 7, 2004.*) The companies outlined how the imputation requirement of Sec. 272(e)(3), as implemented by their proposal, could be operationalized if the Sec. 272 affiliate were integrated into the BOC and discussed how a new rule implementing Section 272(e)(3) would facilitate Commission enforcement. All material shared during the meeting is attached. At the request of staff additional information will be submitted for the record in subsequent filings.

This notice is being filed pursuant to Sec. 1.1206(b)(2) of the Commission's rules. If you have any questions regarding this filing please do not hesitate to contact me.

Sincerely,



Mary L. Henze

cc: W. Dever J. Minkoff
M. Carowitz P. Megna
B. Kehoe D. Cooper
K. Jackson

Post 272 Sunset Implementation of 272(e)(3)

Introduction

Under current FCC requirements (96-150, Accounting Safeguards Order)

- BOC integrated incidental interLATA services are treated as non-regulated for accounting purposes and thus Part 64 allocation rules apply
- Implementation of Sec. 272(e)(3) access imputation requirement is accomplished through existing affiliate transaction rules

As BellSouth proposed in November 2003, FCC must modify rules so that after sunset of Sec. 272

- All BOC integrated interLATA services are treated as regulated for federal regulatory accounting purposes to avoid unnecessary cost allocation
- Implementation of Sec. 272(e)(3) access imputation requirement is accomplished by new rule

Sec. 272(e)(3) is the only post-sunset accounting safeguard required by the Act

Cost Allocation No Longer Valid or Necessary

In establishing original requirement for incidental interLATA services, Commission concluded non-regulated accounting treatment (and resulting Part 64 cost allocation) was necessary to "achieve greater accuracy" than that achieved under Part 36 and Part 69.

In same order, Commission noted "changes in the competitive condition of local telecommunications markets in the future may cause us to reexamine the continued need for our Part 64 cost allocation rules."

Since 1996, the local telecommunications market has become increasingly competitive and the FCC has responded with fundamental changes in interstate regulation and the role that costs play. These include:

- Price cap regulation combined with pricing flexibility has completely eliminated any link between ILECs' recorded costs and the prices they charge for services.
- Elimination of sharing and the low end formula adjustment mechanism (LFAM) which previously created potential incentives for price cap ILECs to shift costs
- Adoption of the CALLS plan under which rates are not based on the development and reporting of costs under any of the Commission's accounting and reporting rules.

Minimal role of costs in today's regulatory environment means "greater accuracy" of cost allocation is no longer necessary.

To avoid unnecessary burden, FCC must determine that integrated interLATA services should be treated as regulated for federal regulatory accounting purposes.

Cost allocation has no bearing on compliance with Sec. 272(e)(3), prevention of cross subsidies, or ratemaking and therefore is unnecessary.

Sec. 272(e)(3) Requirements - Background

Sec. 272 (e)(3) requires BOCs to charge themselves or their 272 affiliates the same price for access that they charge to unaffiliated entities.

In 1996 Accounting Safeguards Order, the FCC:

- Interpreted Sec. 272 (e)(3) “to require the BOCs to charge nondiscriminatory prices ... and to allocate properly the costs of exchange access” according to existing affiliate transactions rules.
- Specifically rejected proposals to use 272(e)(3) to “review the BOC Sec. 272 affiliates’ prices, or profits, or both to ensure that the section 272 affiliates’ prices cover their access charges and all other costs” because such a review would discourage BOCs from competing on price and would conflict with pro-competitive goals of 1996 Act.
- Determined no further rules were necessary to address predatory pricing by BOC 272 affiliates “because adequate mechanisms are available to address this potential problem” including Sections 201 and 202 and antitrust laws.

Since 1996, BOCs have met Sec. 272(e)(3) obligation by imputing access at the line-of-business level as required by FCC’s affiliate transaction rules. Compliance has been audited under 272 Biennial Audit.

Sec. 272 (e)(3) Requirements – Post Sunset

The FCC's original findings regarding Sec. 272(e)(3) are even more valid today as wireline and intermodal competition in local, long distance, and bundled markets has increased. Therefore no dramatic change in Commission approach to implementing Sec. 272(e)(3) is necessary.

To help ensure that Sec. 272(e)(3) continues to be an effective safeguard in a post-272 sunset environment, FCC should adopt a new rule explicitly codifying the language of 272(e)(3), as well as providing accounting guidance.

The text of the rule would read as follows.

53.102 Sec. 272(e)(3) requirements for interLATA activities

The Bell operating company shall charge the 272 affiliate or impute to itself when providing integrated interLATA service an amount for access to its telephone exchange service and exchange access that is no less than the amount charged to any unaffiliated interexchange carriers for such service. Such charges or imputation should be credited to the access revenue account and debited against interLATA revenue.

The appropriate accounts for this transaction are currently within Part 32.

- Part 32.5080 Network access revenue credited
- Part 32.5100 Long distance message revenue debited

Implementation of 272(e)(3) in this manner

- Makes implementation of 272(e)(3) explicit and independent of other rules that may be modified in the future.
- Existence of explicit rule facilitates FCC enforcement under its current authority and complaint processes. In addition, FCC could monitor compliance with new Part 53.102 by requiring BOCs to report the amount of charges and/or imputation to interLATA services in a new schedule in ARMIS Report 43-02.
- Ensures BOCs' interLATA service would be charged the exact same rate for access as other interexchange carriers. Ensures that the BOC LD service has same direct costs as the LD services offered by competitors.